No. 85

In The Supreme Court of the United States

OCTOBER TERM, 1954

UNITED STATES OF AMERICA, *Petitioner*

Versus

R. P. SCOVIL, *ET AL.*

ON WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF SOUTH CAROLINA

BRIEF FOR THE RESPONDENT

J. D. Todd, Jr.,
Greenville, S. C.

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QUESTIONS

I

Whether the priority accorded claims of the United States for taxes against the assets of an insolvent debtor by R. S. 3466 is defeated by a landlord's lien for rent arrears perfected by distress prior to the appointment of the receiver?

II

Whether the lien accorded the United States for unpaid taxes by Section 3670 of the Internal Revenue Code is rendered subordinate to a landlord's lien recognized by state law and perfected by distress because notice of the tax lien was not filed until after the landlord's lien was perfected.

ARGUMENT

I

IS THE PRIORITY ACCORDED CLAIMS OF THE UNITED STATES FOR TAXES AGAINST THE ASSETS OF AN INSOLVENT DEBTOR BY R. S. 3466 DEFEATED BY A LANDLORD'S LIEN FOR RENT ARREARS PERFECTED BY DISTRESS PRIOR TO THE APPOINTMENT OF THE RECEIVER?

The statement of Question One as set forth in the Government's Brief assumes that the Landlord had not divested the debtor of possession of any property subject to the Landlord's lien. Respondent respectfully submits that this assumption is not justified by the record, but that, on the contrary, the record justifies the position that the insolvent debtor had been divested of possession of the property in question when the Receiver was appointed.

The Master, who first heard the case and before whom the Stipulation was made, found that "his landlord's lien as provided by statute, was fully perfected." (R-4) The Master, who incidentally has held that judicial position for the past thirty-four years, had before him at the time of his decision *United States v. Waddil Co.*, 323 U.S. 353, 65 S.Ct. 304, (R-4) which case, as the Government so strongly points out, sets forth the requirements for a specific and perfected lien. It is beyond the realm of reason to suppose that this experienced judge, familiar with the very case relied upon by the Government, would hold the Landlord's lien to be specific and perfected had the Landlord not, prior to the appointment of the Receiver, divested the debtor of possession.

The Circuit Judge likewise found the lien of the Landlord to be specific and perfected. (R-10)

The Government did not except to this concurrent finding by the Master and the Circuit Judge upon its appeal to the Supreme Court of South Carolina. (R-11) The question of the specificity and perfection of the Landlord's lien was not in issue before that Court, having not been raised by the Excep-

tions. *Nally v. Metropolitan Life Insurance Company*, 182 S. E. 301, 178 S. C. 183. The Supreme Court of South Carolina was then quite correct in holding, as it did hold in the opinion below,

> "There is no question in this case of distress having been perfected prior to the appointment of the receiver; therefore the lien was perfected as of that time and the amount specified in such distress was not available to the receiver to pay other debts of the insolvent debtor." (R-13)

The question before this Court then resolves itself into whether the Government's tax lien can be defeated by a prior specific and perfected lien. The Government evidently recognizes that this is the real question before the Court for it argues at length that "this Court has never actually held there is an exception to the absolute priority accorded the United States by the statute." (Page 23, Petitioner's Brief)

Such statement is quite true but this Court has certainly intimated since *Thelusson v. Smith*, 2 Wheat. 396, that if the lien were specific and certain, as we submit it is here, that the Government's priority was subordinated.

The Government states at Page 21 of its Brief:

> "The taxpayer's rights in the property after appointment of the receiver were nil - unless, of course, a surplus should remain after payment of creditors."

Likewise, the taxpayer's rights in the property were nil after the levy of the distress unless a surplus remained after the sale. The taxpayer having no rights in the property at the time of the appointment of the Receiver, the Government could have no rights either.

The learned Attorney General states at Page 21 of the Government's Brief:

> "The United States does not stand in the shoes of the insolvent, and is not claiming under any right of subrogation. It is claiming as a creditor, just as the landlord is, but under a priority granted by Congress, and this Court has never held that Congress, acting

under the powers granted to it by the Constitution, cannot place the debts of the United States ahead of all other debts owing by an insolvent debtor."

This may be true but the Congress, under the Constitution, has not and cannot give the United States a lien against property in the hands of third persons for the tax debt of another. Once the distress was perfected the only claim the United States might have against the property distressed upon would be because of some right the taxpayer might have. He having none, the Government has none.

II

IS THE LIEN ACCORDED THE UNITED STATES FOR UNPAID TAXES BY SECTION 3670 OF THE INTERNAL REVENUE CODE RENDERED SUBORDINATE TO A LANDLORD'S LIEN RECOGNIZED BY STATE LAW AND PERFECTED BY DISTRESS BECAUSE NOTICE OF THE TAX LIEN WAS NOT FILED UNTIL AFTER THE LANDLORD'S LIEN WAS PERFECTED?

We think it may safely be said that the Government's tax lien arising by virtue of Section 3670 was, prior to filing of notice, nothing more than a general, inchoate lien. *United States v. City of New Britain*, 374 U.S. 81, 74 S.Ct. 367. We also think it has been amply demonstrated that the landlord's lien was fully perfected and specific prior to the filing of such notice, and prior to the appointment of the Receiver.

This case is considerably different than *United States v. City of New Britain*, supra, where the Court had before it the question of the priority of two statutory tax liens; that of the United States and that of the City of New Britain. The Court, of course, held that the State of Connecticut could not by statute create a tax lien superior to the tax lien of the United States without the consent of the Congress and that where both liens are general statutory liens, the first in time is the first in right. Here we have no South Carolina statute attempting to give a superior position to a state tax lien at the expense of the Federal Government. Instead, we have a Landlord's lien

recognized since the earliest days of the common law, and affected by the statutory law of South Carolina only in an effort to make its enforcement fairer and more equitable from a procedural standpoint.

Here we have a Landlord who extends credit to his tenant. The tenant fails to pay the rent due for February. The Landlord could immediately distress for this past due rent. A check of the public records would reveal no Federal tax lien which would be paramount to his Landlord's lien. Secure in the knowledge that his lien is a first lien against all the chattels of his tenant, he is tolerant of his tenant. He does not immediately close him up and put him out of business. Instead, he extends him further credit for March and a portion of April. When finally it becomes evident the tenant will not or cannot pay the agreed upon rent, he converts his inchoate Landlord's lien into a specific and perfected lien by distress. Why then is he not a "purchaser" within the meaning of the Section 3672 as the Master, the Circuit Judge and the Supreme Court of South Carolina held?

In *National Refining Co. v. United States*, 160 F. (2d) 951, the Court of Appeals for the 8th Circuit said:

> "We think it is safe to say that one who for a valuable present consideration, acquires property or an interest in property is a 'purchaser' within the meaning of 26 USCA Int. Rev. Code, 3672."

The Landlord gave consideration by the use of the premises (especially after default in payment of the rent) and acquired an interest in the specific property by distress before the Government saw fit to give notice of its secret lien. Incidentally, it is appropriate to point out that the Government saw fit to keep its lien secret for some thirteen months. Certainly, in view of such dilatory action on the part of the Collector of Internal Revenue the Government is in no position to complain.

In *Hawkins v. Savage*, 110 F. Suppl. 615, it was stated:

> "Section 3672 was enacted to protect what are

> commonly known as innocent purchasers for value, the word 'purchasers' embracing all those classes of persons who deal in the property of a debtor while other and secret liens against the property may exist."

Crawford Co. v. L. Leopold and Co., 70 N.Y.S. (2d) 183, affirmed 297 N.Y. 884, 79 N.E. (2d) 279; *Grossman v. City of New York*, 66 N.Y.S. (2d) 363, *United States v. Rosebush*, 45 F. Suppl. 664, all seem to be authority for the Landlord's position in this case.

The Landlord was a "purchaser" within the meaning of Section 3672 at the time the Government gave notice of its tax liens by filing. On some of these claims the assessment lists had been received in the Collector's Office more than a year prior to the levy of the distress by the Landlord. Even the slightest diligence on the part of the Government would have given notice to the Landlord that he could not depend upon the property of the tenant on the premises for satisfaction of any unpaid rent. He could have protected himself by prompt action upon the first default in the payment of the rent. Lulled into a false sense of security, he extended credit on the faith of ample property available for the satisfaction of his debt. Equity, good conscience and the terms of the statute require that he be protected as a "purchaser".

CONCLUSION

There is no error in the decision of the Court below and it should be affirmed.

Respectfully submitted,
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Attorney for Respondent